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Online dispute resolution for cross-border electronic commerce transactions

Proposal by the Governments of Colombia and the United States of America

Note by the Secretariat

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1. The Governments of Colombia and the United States of America welcome the call for the Working Group to consider payment chargebacks as part of its work in developing instruments relating to online dispute resolution of low-value cross-border e-commerce consumer disputes. We propose that Working Group III link any non-binding recommendation under Track II of the Rules to a uniform mandatory payment system chargeback requirement.

I. Background

2. Working Group III is currently engaged in work on a two-track system, one track that would end in binding arbitration (Track I) and another that would end in a non-binding recommendation (Track II).

3. The delegations of Colombia and the United States believe that in order for any non-binding recommendation to provide sufficient consumer protection, the recommendation would need to be legally linked to the same money transfer payment channel as the original payment, given the general lack of judicial remedies in cross-border e-commerce transactions.[1] As the ODR colloquium that lead to the establishment of the Working Group highlighted, all the successful ODR programs of the last decade have been where enforcement of the outcome comes through the same money channel as the original payment.[2]

4. At its May 2013 session, the Working Group requested that the Secretariat provide an overview of private enforcement mechanisms, in the context of compliance with a neutral's non-binding recommendation under Track II of the draft rules. A/CN.9/769, paragraphs 57 and 58. In response, the Secretariat prepared a paper addressing inter alia how chargebacks might be integrated into the procedural framework of the rules. A/CN.9/WG.III/WP.124, paragraphs 35-39 and 44.

5. At its October 2014 session, the Working Group decided to further examine the issue of private enforcement mechanisms in the context of the various formulated proposals. The Working Group specifically requested that the Secretariat prepare additional materials on chargebacks. The Government of Colombia further stated that it would submit a proposal for the February 2015 session of the Working Group concerning chargebacks, which, it pointed out is a private enforcement mechanism, practical and effective. A/CN.9/827, paragraphs 53 and 95.

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[1] A paper co-sponsored by the delegations of Colombia, Honduras, Kenya and the United States (A/CN.9/WG.III/WP.125) explains that arbitration is generally more consumer protective than a non-binding recommendation in cross-border transactions, given that court remedies are not generally available or may be impractical. ODR with binding arbitration as a "backstop" serves as a strong incentive to move the parties to voluntary resolution through negotiation or facilitated settlement.

[2] As discussed at the UNCITRAL ODR colloquium, PayPal and eBay have a private contractual form of chargebacks if the purchaser did not receive the product or it was not what was ordered. The dispute is resolved under the terms of the private contract with the merchant. This private system works because vendors maintain accounts with eBay and PayPal and funds can be frozen and automatically transferred consistent with the decision. Enforcement is similar to the ICANN Dispute resolution model in that ICANN under the terms of the contract can unilaterally change domain name registries. Report of UNCITRAL ODR colloquium, A/CN.9/706, paras. 30 and 43.

II. Payment system chargebacks provide a powerful tool for resolution of cross-border e-commerce disputes

6. Chargebacks provide a flexible and effective legal framework for dealing with low-value cross-border e-commerce disputes, especially when coupled with an online dispute resolution mechanism, like the draft UNCITRAL ODR Rules. A chargeback legal framework provides many benefits including: (1) mandatory application to vendors through use of a payment channel (rather than voluntary application based on a private agreement with a specific ODR provider); (2) buyers may opt into the system post-dispute; (3) buyers do not waive court remedies; and (4) enforcement of a decision is guaranteed cross-border without costly court intervention.

7. The 1999 OECD Guidelines on E-Commerce recommend the use of "limitations of liability for unauthorized or fraudulent use of payment systems, and chargeback mechanisms [as] powerful tools to enhance consumer confidence." Available at www.oecd.org/dataoecd/18/13/34023235.pdf at 7.

8. These ADR/payment protections enhance consumer confidence in the use of payment cards for online purchases and in the global marketplace more generally.

9. Chargebacks can be a particularly effective tool when e-commerce transactions are conducted cross-border. The OECD has concluded that:

> These protections can be valuable to consumers when dealing with uncooperative businesses and play a particularly important role in distance and cross-border transactions where it may be difficult to communicate with or take legal action against the business.

Consumer Dispute Resolution and Redress in the Global Marketplace, at 6, available at, www.oecd.org/sti/consumer/36456184.pdf.

III. Payment system chargebacks not limited to credit cards

10. The Secretariat concluded (A/CN.9/WG.III/WP.124, para. 44) that "chargebacks, while a useful model, may be limited in their utility given that they apply only to payments made with a credit card." Nonetheless, in both the Colombian and United States chargeback legislation, payment card chargebacks are not limited to credit cards.

11. Colombia has a new consumer protection law that provides for chargebacks for all types of payments including credit cards, debit cards and other electronic payments. The statute sets up an automatic reversal of payment if the consumer reports to the provider and issuer within five days of notice of any claim, essentially shifting the burden to the provider or issuer. The chargeback is broadly applicable to any e-commerce transaction involving the sale of goods or performance of services. Colombia is developing an ODR mechanism to resolve the disputes arising from the application of the automatic chargebacks. The Colombian law is further described in annex A.

12. United States law provides consumers with protections for online purchases via payment card chargebacks. For example, credit card issuers must consider the

claims of the consumer for unauthorized or fraudulent charges, and non-delivery or non-conforming goods. Debit card issuers must consider more limited claims, including unauthorized or fraudulent charges. As a matter of practice, most United States payment card networks provide the same chargeback rights on consumer disputes as with credit cards. The law requires credit and debit card issuers to suspend disputed charges and conduct an investigation involving both consumers and merchants. If they sustain the consumer's claim, they must reverse the disputed charge.

13. Under United States law, consumers have the option to exercise these protections, which cannot be waived. The result is non-binding, in that the consumer retains its rights to seek redress in a court. The chargeback law extends to both domestic and cross-border purchases.

14. A proposed model law on payment system chargebacks has been submitted in the OAS CIDIP VII negotiations. The draft model law would provide for chargebacks for both credit and debit card payments for goods and services that are: (a) unauthorized; (b) incorrect in amount; (c) not accepted by the consumer or not delivered in accordance with the terms of the contract. The protection would extend to cross-border purchases and mobile payments to the extent they are linked to debit or credit cards. See *Draft Model Law: Alternate Dispute Resolution for Consumer Payment Card Claims*, available at www.oas.org/dil/esp/CIDIPVII_proteccion_al_consumidor_united_states_guia_legislativa_anexo_B.pdf.

15. The UNCITRAL ODR colloquium also considered a proposal for a model law on chargebacks, drawing from elements of the OAS chargeback proposal, including scope. The UNCITRAL proposal, like the Colombian law, would extend to all types of payments. See http://law.pace.edu/lawschool/files/iicl/odr/MacCarthy.ppt; report of UNCITRAL ODR colloquium, A/CN.9/706, paragraph 43.

IV. A model law on payment system chargebacks would be consistent with the ODR Rules

16. The scope of the Colombian, United States and proposed OAS chargeback legislation is substantially identical to the scope of the Draft Model Rules under article 1(2) for both Track I and II, i.e., "not delivered, not timely delivered, not properly charged or credited, or not provided in conformity with the sales or service contract." As the Working Group has concluded, this scope covers the most common complaints concerning cross-border e-commerce consumer transactions. Decisions involving these disputes may be readily resolved through ODR linked to payment system chargebacks since the claims are focused and fact-based and involve a limited set of remedies.

V. Conclusion

17. In conclusion, we welcome the call for consideration of payment system chargebacks as a tool for providing effective enforcement of outcomes under the draft rules. It is a priority that Working Group III create a work product that casts a

broader enough net to capture the largest number of e-commerce disputes and offers effective and immediate consumer protection in cross-border e-commerce transactions.

18. The essence of the payment system chargeback is represented in the process that this Working Group has established for Track II leading to a non-binding recommendation. It is appropriate that this Working Group consider the incorporation of a chargeback system, given its mandate to create model rules and consider private enforcement mechanisms.

Annex A

The reversal mechanism of payment in the Colombian legislation[3]

When the holder of a credit or debit card justifiably questions a transaction that has already been paid, the corresponding amount is deducted from the account of the establishment that made the transaction. This deduction is called "a *chargeback*" in English and "une *rétrofacturation*" in French. While the websites of credit card issuers do not provide a Spanish term, their Mexican, Argentine, Chilean, American, etc. equivalents unanimously regard it as a "*Contracargo*". According to Visa International, the correct term in Spain is "*retroceso*". Spanish banks prefer "*retrocesión*".[4]

- The credit and debit card system

Means of payment such as cash, checks, debit and credit cards or online payment mechanisms are referred to as "two-side" or "two platform" markets. What differentiates a one-side market from a two-side market is that (a) there are two distinct groups of customers; (b) they are interdependent, meaning that monies are transferred from one group to the other; and (c) an intermediary operates the transfer from one group to the other.

The costs that cardholders must assume, as a general rule, for purchasing goods and services through credit cards are: *monthly (or quarterly) fixed charges, handling fee and interest*. The costs associated with purchases vary depending on the issuing bank of the card. Commercial establishments charge an acquiring commission.

- Networks and other market players

The systems of electronic payment through cards provide an alternative to cash while decreasing transactions costs. Networks or platforms operate as open or closed systems.

Open systems are comprised of:[5] the cardholder, the merchant, the cardholder's bank, the merchant's bank and the network operator (e.g. Visa or MasterCard).[6]

In open systems, the cardholder pays a commercial establishment for goods or services using a debit or credit card. The merchant charges the card through a POS terminal which communicates the cardholder's information (e.g. PIN) and the value of the transaction to the merchant's bank.

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[3] The Chargeback mechanism only operates when the sale of goods is carried out through electronic commerce mechanisms, such as Internet, PSE and/or call centre and/or any other teleshopping or online store mechanism, and when a credit card, debit card or other electronic payment instrument, has been used for the payment.

[4] In: http://ec.europa.eu/translation/bulletins/puntoycoma/70/pyc701.htm.

[5] Article 1 of Decree 2230 of 2006.

[6] The cardholder's bank and the merchant's bank can be the same bank.

The merchant's bank queries the network, which consults the cardholder's bank to obtain verification and authorization as to whether the cardholder has adequate funds to complete the transaction. If the cardholder has sufficient funds, the transaction is authorized and the cardholder's bank transfers funds to the account of the merchant in the merchant's bank in an amount equal to the sale price minus the value of the Interbank Exchange Rate (TII).[7] The merchant's bank pays the merchant the selling price minus the value of the Acquiring Commission. After the merchant receives confirmation of the deposit, the merchant delivers the goods or services to the cardholder.

When a cardholder makes a purchase at a business establishment using a credit or debit card, the networks are responsible, through their technology infrastructure, for sending the transaction's information to the cardholder's bank and to authorize or reject the transaction. The networks receive a commission from the system's participants.[8]

The networks or payment platforms operating in an open system are Administrator Entities of Low-Value Payment Systems, whose business is the management and operation of one or more low-value payment systems. These entities are regulated by Article 2.17.1.1.1 of Decree 2555 of 2010,[9] amended by the National Decree 3594 of 2010, Added by National Decree 4809 of 2011, Added by National Decree 0848 of 2013.

Closed systems have a very similar process to open systems, but with fewer steps since there are fewer agents participating. Closed systems are comprised of: the cardholder, the merchant, and the payment network or platform. In these systems, there are usually no cardholder banks or merchant banks acting independently, as these roles are carried out by a banking institution that enrols the cardholder and merchant in the system, issues the card and is identified as the acquirer of the transaction made with the card.

- Chargeback mechanism

The reversal in payment, or chargeback, involves a number of commissions and fees, which must be returned to the consumer, in addition to the price.

Document A/CN.9/WG.III/WP.124 of Working Group III — UNCITRAL, includes a discussion of a mechanism on *reversal of payment* or "*chargeback*", "*reimbursement*" or "*return*" by which the participants in a process of payment through electronic means, shall reimburse the sums of money cancelled or debited to the consumer, when certain events occur and the request is made within a period of time laid down in law. This mechanism will be reviewed by the delegations.

This mechanism is intended for cross-border e-commerce transactions involving a credit card, debit card or other electronic payment method.

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[7] The cardholder's bank responds to the transaction made by the cardholder within 48 hours of the operation, even if the debt is cancelled.

[8] Article 2.17.1.1.1 of Decree 2555 of 2010.

[9] Decree 2555 of 2010 "*Whereby are collected and re-issued rules on the financial, insurance and stock market sector and dictate other provisions.*"

In 2011, the Colombian Congress issued Law 1480, "*Whereby the Consumer Statute is issued and dictate other provisions*". Under article 51 of this law a chargeback mechanism is established that allows the return of payments when:

1. Sales of goods are offered through electronic commerce, such as Internet, PSE[10] call centres or any other mechanism for teleshopping via an online store, and
2. Payment has been made by a credit card, debit card or any other electronic payment method.

Under this provision, the participants of the payment process are required to reverse the payments at the request of the consumer when:

1. The transaction is fraudulent or was unsolicited
2. The product was not received
3. The delivered product does not correspond to the product ordered or is defective.

Under Colombian law, a chargeback request is effective if the consumer[11] informs the issuer of the electronic payment used and the merchant within five (5) business days from the date of (1) the receipt of any report of fraudulent or unsolicited merchandise, (2) the date the product should have been received in the event of non-delivery or (3) when the product was received in the event the product was defective or did not correspond to the product ordered. Upon receipt of a complaint, the issuer of the electronic payment instrument used, together with the other **participants in the payment process**,[12] shall reverse the transaction to the purchaser.

The regulations implementing the Colombian law also stipulate the period within which the complaint or demand must be filed before the competent judicial or administrative authority.

This reversion must be implemented without prejudice to the duty of the provider to meet its legal and contractual obligations to the consumer. Administrative sanctions may apply, if the judicial or administrative authority determines that there was bad faith on the part of the consumer, in which case the Superintendence may impose penalties of up to fifty (50) minimum monthly legal wages.

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[10] "Pagos Seguros en Linea-PSE". This mechanism allows companies to offer their customers the possibility of making payments and/or purchases, debiting the amount online from the Financial Entity where the client has their money, and depositing it in the acquiring Financial Entity that determines the company or commerce.

[11] N. 3 article 5, Law 1480 of 2011 "*Consumer or user. Any natural or legal person that, as an end user, purchases, possesses or uses a particular product, whatever its nature, to satisfy a personal, private, family or home and business need when it is not intrinsically linked to his economic activity. Consumer will be understood to be included in the definition of the term user.*"

[12] "**Paragraph 1**. For the purposes of this article, are understood by participants in the payment process, the issuers of the payment instruments, the administering entities of the Low-Value Payment Systems, banks that manage the accounts and/or consumer bank deposits and/or supplier, among others."

Under Article 51 of Law 1480 of 2011, paragraph 2, the consumer is entitled to reverse the payments for any service or obligation of periodic compliance, for any reason and even without there being any justification, provided that the payment is made through an automatic debit operation previously authorized by that consumer, in the terms established by the National Government.

The reversal in payment — or as it is known in Colombia, "refund" or "chargeback" — involves all actors linked in the payment process through electronic means, in both open and closed systems: **the issuing bank**, **the acquiring bank**, **the merchant**, **the cardholder and the network or system administrator of low-value payments**, who are subject to obligations and rights.

Such a mechanism provides the consumer with a solution to their dispute in a quick and efficient manner, without renouncing the recourse to traditional judicial justice.

This non-binding chargeback mechanism can be linked to the procedure provided by ODR, leaving the consumer with the possibility of using the two Tracks laid down in the draft rules, or traditional judicial justice.